MASB MALAYSIAN ACCOUNTING STANDARDS BOARD
LEMBAGA PIAWAIAN PERAKAUNAN MALAYSIA

9 November 2010

Sir David Tweedie
Chairman
International Accounting Standards Board (IASB)
30 Cannon Street
London ED 4M 6 XH
United Kingdom

Dear Sir David

IASB EXPOSURE DRAFT – RECOVERY OF UNDERLYING ASSETS (PROPOSED AMENDMENTS TO IAS 12)

The Malaysian Accounting Standards Board welcomes the opportunity to provide comments on the IASB Exposure Draft – Recovery of Underlying Assets (Proposed Amendments to IAS 12).

We appreciate the IASB's efforts to provide an exception to the principle of IAS 12 that the measurement of deferred tax liabilities and deferred tax assets should reflect the tax consequences that would follow from the manner in which the entity expects to recover or settle the carrying amount of its assets and liabilities.

However, having reviewed the draft IFRS, we are not convinced the proposal will result in the financial statements providing better quality information to users.

The proposed exception would create an inconsistency in the application of the fundamental principle of IAS 12 and the reasons provided in the ED are not sufficiently persuasive to warrant an exception to be given to specified assets measured at fair value from applying the said principle. In our view, if significant judgement has been used in determining the expected manner of recovery of these assets, additional disclosures could be made in the financial statements to provide users with the relevant information.

Our detailed responses are enclosed in the Appendix of this letter.

If you need further clarification, please contact Ms Tan Bee Leng at +603 2240 9200 or by email at beeleng@masb.org.my.

Thank you.

Yours sincerely,

Mohammad Faiz Azmi
Chairman

Appendix

Question 1 – Exception to the measurement principle

The Board proposes an exception to the principle in IAS 12 that the measurement of deferred tax liabilities and deferred tax assets should reflect the tax consequences that would follow from the manner in which the entity expects to recover or settle the carrying amount of its assets and liabilities. The proposed exception would apply when specified underlying assets are remeasured or revalued at fair value.

Do you agree that this exception should apply when the specified underlying assets are remeasured or revalued at fair value? Why or why not?

We do not support the proposed exception.

The justification provided in the ED is not conceptually supportable and is in fact flawed. Deferred tax is measured based on the manner the entity expects to recover or settle the carrying amount of its assets. The accounting policy choice of an entity of measuring its assets using either the cost model or the revaluation model has no correlation as to how an entity expects to recover its assets and liabilities. It is fundamentally flawed to presume that if an entity opted for the revaluation model, the assets will be recovered through sale. As such, the information produced is less likely to be useful to users of financial statements.

Whilst we agree with the Board's observation that in some cases it may be difficult or subjective to determine the expected manner or recovery of an asset with mixed-use, we are not convinced this reason justifies the proposed exception. There are many other areas of accounting where preparers have to exercise significant judgement but no exceptions were given in IFRSs. In our view, the exercise of judgement and estimates are inherent attributes in the application of IFRS and if significant judgement has been used in determining the expected manner of recovery of a mixed-use asset, additional disclosures could be made in the financial statements to provide users with the relevant information.

Moreover, we believe it may also be equally difficult or subjective to determine the expected manner of recovery of mixed-use assets measured at cost. Therefore, should the Board decide to proceed with the proposal, we see no reason why assets measured at cost are not accorded similar exception.

For property, plant and equipment or intangible assets measured using the revaluation model, we are concerned that the proposed exception will create anomaly with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations. *Under IFRS 5, a non-current asset is classified as held for sale only when its sale is highly probable and they would be measured at the lower of its carrying amount and fair value less costs to sell. On the other hand, the ED proposes to apply a rebuttable presumption that the carrying amount of these assets will be recovered entirely by sale unless there is clear evidence that it will consume the asset's economic benefits throughout its economic life - in other words these assets are deemed to be recovered by sale by virtue that they are measured at revaluation. The anomaly herein are twofold: (i) whether the measurement basis of these assets would be subject to that of IFRS 5 or IAS 16 for property, plant and equipment or IAS 38 for intangible assets; and (ii) no explanation has been provided to clarify as to why the basis upon which these assets will be recovered through sale is different from IFRS 5. We therefore urge the Board to seriously reconsider its decision.*

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Appendix

Question 2 – Scope of the exception

The Board identified that the expected manner of recovery of some underlying assets that are remeasured or revalued at fair value may be difficult and subjective to determine when deferred tax liabilities or deferred tax assets arise from:

(a) investment property that is measured using the fair value model in IAS 40;

(b) property, plant and equipment or intangible assets measured using the revaluation model in IAS 16 or IAS 38;

(c) investment property, property, plant and equipment or intangible assets initially measured at fair value in a business combination if the entity uses the fair value or revaluation model when subsequently measuring the underlying asset; and

(d) other underlying assets or liabilities that are measured at fair value or on a revaluation basis.

The Board proposes that the scope of the exception should include the underlying assets described in (a), (b) and (c), but not those assets or liabilities described in (d).

Do you agree with the underlying assets included within the scope of the proposed exception?

Why or why not? If not, what changes to the scope do you propose and why?

As mentioned in our response to Question 1, we do not support the proposed exception. Therefore we do not agree with the proposed scope of the exception.

In particular, we believe the expected manner of recovery for property plant and equipment is mainly through use rather than through sale of assets. Therefore the exception would create an inconsistency with the expected manner of recovery determined by management.

For assets described in (d), we find it anomalous that the proposed exception does not apply to them (e.g. financial instruments in IAS 39 Financial Instruments: Recognition and Measurement *and biological assets in IAS 41* Agriculture*). We are not convinced with the rationale provided by the Board in this regard.*

Question 3 – Measurement basis used in the exception

The Board proposes that, when the exception applies, deferred tax liabilities and deferred tax assets should be measured by applying a rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely through sale. This presumption would be rebutted only when an entity has clear evidence that it will consume the asset's economic benefits throughout its economic life.

Do you agree with the rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely by sale when the exception applies?

Why or why not? If not, what measurement basis do you propose and why?

As mentioned in our response to Question 1, we do not support the proposed exception and the proposal may be inconsistent with IFRS 5.

Nevertheless, should the Board decide to proceed with its proposal to introduce an exception, we disagree with the rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely by sale. As mentioned in our response to Question 2, we believe the expected manner of recovery for property, plant and equipment is mainly through use rather than through sale. We therefore recommend the rebuttable presumption to be redrafted ie that the asset will be recovered through use when it is difficult and subjective to determine the manner of recovery.

Alternatively the Board could consider requiring fall back to the guidance in paragraph 10 of IAS 12 when it is difficult and subjective to determine the manner of recovery of the asset. In this regard, Paragraph 10 clarifies that where the tax base of an asset or liability is not immediately apparent, the entity should consider the fundamental principle of IAS 12 i.e. the entity, with certain limited exceptions, recognise a deferred tax liability (asset) whenever recovery or settlement of the carrying amount of an asset or liability would make future tax payments larger (smaller) than they would be if such recovery or settlement were to have no tax consequences. In our view, requiring a fall back to paragraph 10, rather than the proposed exception, would be consistent with the guidance in IAS 8 paragraph 10 which requires an entity to develop and apply accounting policy that results in information that are, amongst others, prudent for users of financial statements.

However, if the rebuttable presumption is not redrafted, we are concerned that there may be divergent views in the interpretation of 'clear evidence'. Some may interpret that the presumption is only rebutted when there is documentary evidence to indicate the management's expectation not to sell the asset, whilst others may interpret otherwise. Hence the Board should reconsider its proposal and there ought to be greater clarity or relevant examples of 'clear evidence' to avoid any divergent interpretation.

It is also not clear whether 'entirely' refers to the class of assets or individual assets and we request the Board to clarify its meaning in this regard.

Question 4 – Transition

The Board proposes that the amendments should apply retrospectively. This requirement includes retrospective restatement of all deferred tax liabilities or deferred tax assets within the scope of the proposed amendments, including those that were initially recognised in a business combination.

Do you agree with the retrospective application of the proposed amendments to IAS 12 to all deferred tax liabilities or deferred tax assets, including those that were recognised in a business combination?

Why or why not? If not, what transition method do you propose and why?

We disagree with the proposal to apply the amendments retrospectively.

In our view, it is difficult and not practical to require a retrospective application to assets measured at fair value acquired in a business combination. Adjustments will need to be made to goodwill and negative goodwill including impairment on goodwill. In this regard, we propose that the amendments, if adopted, be applied prospectively.